

GAO

Testimony

Before the Subcommittee on Department Operations, Research,
and Foreign Agriculture, Committee on Agriculture, House of
Representatives

For Release on Delivery
Expected at
9:30 a.m., EDT
Tuesday
July 28, 1992

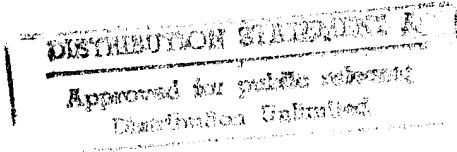
AGRICULTURAL TRADE

High-Value Products and U.S.
Export Promotion Efforts

Statement of Allan I. Mendelowitz, Director
International Trade and Finance Issues
General Government Division



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AGRICULTURAL TRADE
HIGH-VALUE PRODUCTS AND U.S. EXPORT
PROMOTION EFFORTS

SUMMARY OF STATEMENT OF ALLAN I. MENDELOWITZ
DIRECTOR, INTERNATIONAL TRADE AND FINANCE ISSUES
GENERAL GOVERNMENT DIVISION

This testimony addresses issues related to H.R. 4279. This bill establishes percentage goals for assisting high-value agricultural product exports under the Department of Agriculture's (USDA) Export Enhancement Program and export guarantee programs.

The Food, Agriculture, Conservation, and Trade Act of 1990 required USDA to develop a long-term agricultural trade strategy and report to Congress on it by October 1991. This strategy has not yet been completed. Without such a plan the USDA's individual export promotion activities will continue to lack a coherent rationale and justification. Furthermore, U.S. government export promotion programs are not funded on the basis of any government-wide strategy or set of priorities. Consequently, taxpayers do not have reasonable assurances that the government's resources are being effectively used to emphasize sectors and programs with the highest potential return.

The level of support and specific type of program to assist high-value product exports are presently not based on an overall strategy that, in turn, is one component of a government-wide export promotion strategy. Adherence by the Department of Agriculture to the bill's percentage goals may not represent a good use of program funds.

There are good reasons for the government to be interested in promoting the export of high-value products, but there is considerable confusion over the nature of the economic benefits of HVP exports. Although a 1989 Department of Agriculture Economic Research Service study is frequently cited to support the proposition that the economic benefits of high-value export promotion exceed those of bulk exports, the analysis does not support such a conclusion. The claimed benefits are based on key assumptions that render the study's conclusions unrealistic. Therefore, the study should not be used as the primary basis for government export assistance to high-value products.

Promoting high-value products has merit, but the amount of federal funds to be spent on high-value product export assistance and the way in which they should be used should not be determined in isolation. A long-term agricultural trade strategy must be developed and integrated into a comprehensive, government-wide export promotion plan in order to assure that public funds are effectively spent.

Mr. Chairman and Members of the Subcommittee:

I am pleased to be here today to discuss the government's role in exporting high-value agricultural products. Specifically, I would like to comment on issues related to H.R. 4279. This bill defines "processed" and "high-value" agricultural products and establishes set-asides for these products. These set-asides seek to ensure, to the extent practicable, that those products receive 35 percent of export credit guarantees issued by the Department of Agriculture's (USDA) Commodity Credit Corporation and 25 percent of the bonuses awarded under its Export Enhancement Program (EEP). My comments are based on prior GAO reports on USDA export programs and governmentwide export promotion programs, and our ongoing work on high-value products (HVP).¹

While we do not agree that a widely cited 1989 USDA Economic Research Service (ERS) study² supports the conclusion that the economic multiplier generated by exporting HVPs greatly exceeds that from exporting bulk commodities, there are a number of good reasons why HVP exports should be considered by the U.S. government for export promotion assistance.

. The HVP share of world trade was about \$160 billion in 1990, which represents about 75 percent of global agricultural trade.³

. World HVP trade is continuing to grow more rapidly than bulk trade, although HVP exports are expanding more slowly than world trade in nonagricultural products. And, HVP export growth is expected to continue as world income rises. It makes sense to pursue growing markets.

. HVP products are more easily differentiated through advertising, marketing, and product development. These are activities in which the United States may have a comparative advantage.

¹U.S. Department of Agriculture: Strategic Marketing Needed to Lead Agribusiness in International Trade (GAO/RCED-91-22, Jan. 22, 1991); International Trade: Competition for Japan's High Value Agricultural Market (GAO/NSIAD-90-134, Mar. 30, 1990); and International Trade: Foreign Market Development for High Value Agricultural Products (GAO/NSIAD-90-47, Jan. 17, 1990).

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²Gerald Schluter and William Edmondson Exporting Processed Instead of Raw Agricultural Products, U.S. Department of Agriculture, Economic Research Service, Staff Report No. AGES 89-58 (Washington, D.C.: Nov. 1989).

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³Intra-European Community (EC) trade is excluded from these statistics. If intra-EC trade is not excluded, the HVP share of world trade is about \$256 billion in 1990, which represents about 80 percent of global agricultural trade.

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- . Some HVP products may be subject to fewer swings in price and demand as compared to bulk products, and thus may offer more stable market outlets.
- . Promoting HVP exports offers the United States an opportunity to redirect its approach to agricultural exports from a production orientation, which moves surplus production to overseas markets, toward one that is market based and responsive to international demand and U.S. competitiveness.

The United States spends significantly more on promoting high-value agricultural products than most of its competitors, however, these competitors appear to receive a greater return on their marketing investment. Many of our competitors--EC nations in particular--have developed considerable expertise in identifying markets and emphasizing the use of market research to tailor promotions to consumer demand.

It is important to note that without a comprehensive strategic plan for promoting all U.S. exports, including agricultural products, the U.S. government may find it difficult to effectively use the public resources devoted to export promotion. Therefore, we believe that narrowly focused export promotion initiatives should not be considered outside the framework of such a plan. Such a plan has yet to be developed either government-wide for U.S. exports or within USDA for agricultural exports.

BACKGROUND

High-value agricultural products include a wide variety of items, most of which have value added to their original state through specialized handling, transportation, marketing, processing, or

packaging. Some products are considered highly processed HVPs. These include prepared meat, milk, butter, and cereal preparations, and preserved fruits and vegetables. Others are considered semiprocessed HVPs. These include wheat flour, oilseed cake and meal, and vegetable oil. However, not all HVPs receive this designation because of processing. For example, fresh fruits and vegetables are categorized as HVPs because the raw commodity has an intrinsically high value.

Bulk commodities, which are raw agricultural products, have little value added after the farm gate besides relatively uncomplicated transportation and handling costs. Some typical bulk commodities are wheat, corn, rice, oilseeds, raw tobacco, and raw cotton. Over the years, bulk commodities have made up the largest portion of U.S. agricultural exports.

Presently, HVPs constitute a growing proportion of world agricultural exports. But they have historically formed less than half of U.S. agricultural exports. Competition is strong in HVP markets, and the United States and the European Community, the U.S.' largest competitor, both use government programs to promote exports. Over the past three decades, the U.S. share of world HVP exports, excluding intra-EC trade, has increased from 10.8 percent in 1962 to 15.6 percent in 1990. The EC's share increased from 13.5 percent in 1962 to 20 percent in 1990.

THE IMPORTANCE OF A STRATEGIC EXPORT PROMOTION PLAN

The United States spends considerable money on export promotion. However, there is no national strategy that guides how these funds are used. Furthermore, despite a requirement in the Food, Agriculture, Conservation, and Trade Act of 1990 that USDA prepare a "long-term agricultural trade strategy," USDA has yet to complete this important task. Consequently, taxpayers do not have reasonable assurances that the considerable public funds expended on export promotion are being effectively used to emphasize sectors and programs with the highest potential returns.

In evaluating the USDA's export promotion activities, it is important to examine how they fit into governmentwide efforts to promote U.S. products in world markets. Presently, 10 federal government agencies offer programs to help businesses begin exporting or to expand their exports. In fiscal year 1991 these agencies spent about \$2.7 billion on export promotion programs and approved about \$21.4 billion in export loans, credit guarantees, and insurance. However, these export promotion programs are not funded on the basis of any governmentwide strategy or set of priorities. For example, while agricultural products constitute only about 10 percent of U.S. exports, USDA spent about \$2 billion on export promotion in fiscal year 1991. In other words, USDA spent almost three-quarters of the government's outlays on export promotion.

In our recent report to the House Committee on Government Operations reviewing the resources of all federal government agencies involved in export promotion, we recommended that Congress require all export promotion programs to be integrated into a governmentwide strategic plan and funded in a manner consistent with the priorities given them under the plan. We believe that implementation of this recommendation will help assure that U.S. export promotion programs are carried out in a manner that maximizes their potential for contributing to the U.S. economy. The government's present approach to export promotion lacks coherence because no overall strategy and set of priorities exist to guide agency efforts.

USDA STILL LACKS A STRATEGIC PLAN

The Food, Agriculture, Conservation, and Trade Act of 1990 required USDA to develop a long-term agricultural trade strategy, and required a report to Congress on the long-term trade strategy by October 1, 1991. Specifically, the act provided that the strategy should be designed to ensure

- . the growth of exports of U.S. agricultural commodities,
- . the efficient, coordinated use of federal programs designed to promote the export of U.S. agricultural commodities,
- . the provision of food assistance and the improvement in the commercial potential of markets for U.S. agricultural commodities in developing countries, and
- . the maintenance of traditional markets for U.S. agricultural commodities.

In addition, the act mandated that USDA designate priority growth markets and devise individual market development plans for each priority market.

More than a year ago I testified before this Subcommittee that the USDA's Agricultural Marketing Service and Foreign Agricultural Service (FAS) were in the final stages of developing new strategic plans.⁴ These plans were expected to (1) adapt their programs to changing economic conditions, (2) ensure the most effective use of resources, and (3) strengthen the integration of strategic marketing activities. USDA appointed FAS as the lead agency to prepare the required multiyear agricultural trade strategy, as specified under the 1990 legislation. This was a logical choice, given the FAS' responsibilities in promoting agricultural exports, including HVPs. The FAS' High Value Products Service Division is

⁴U.S. Efforts to Increase Exports of High Value Agricultural Exports (GAO/T-NSIAD-91-43, June 25, 1991).

responsible for developing and implementing policies, services, and programs for HVPs.

Despite last year's expectations, the plan has not been completed. According to USDA officials, efforts to complete it have foundered because of methodological weaknesses and conceptual deficiencies. On February 24, 1992, USDA notified Congress that it does not plan to publish a long-term agricultural trade strategy report, but will continue to work on developing this strategy.⁵ The lack of progress by USDA in completing a long-term agricultural trade strategy to guide the funding, design, administration, and organization of its agricultural export efforts is unfortunate. Without such a plan it is difficult to establish what support USDA should give to HVP exports.

IMPLICATIONS OF H.R. 4279 FOR U.S. AGRICULTURAL TRADE

The declared policy of H.R. 4279 is that the U.S. share of world trade in processed and high-value agricultural products be not less than 15 percent. If intra-EC trade is excluded from the volume of world trade, as we believe is appropriate, then this goal was already accomplished in 1990. The USDA's Economic Research Service recently estimated that U.S. HVP exports accounted for 15.6 percent of world HVP trade in 1990.

Of some concern to us is the potential that USDA will not use its export promotion budget effectively in response to the bill's percentage goal for HVP export assistance. As I stated earlier, we believe there are good reasons to support increases in HVP exports. However, the level of support and the specific types of programs to assist HVP exports should be based on an overall agricultural trade strategy that, in turn, is one component of a governmentwide export promotion strategy. EEP and the Export Credit Guarantee Programs (General Sales Manager-102 and -103) may not be the best way to assist HVP exports. By mandating that a set percentage of the programs be made available for HVPs, there is no assurance that the funds will be spent as effectively as possible. Attractive export opportunities in bulk commodities may be foregone in order to maintain the minimum proportion of assistance sought in the act for HVPs. Or, assistance to HVP exports that do not represent a good use of program resources may be made simply to maintain the ratios. Our reviews of the Targeted Export Assistance program and the

⁵USDA invoked the "scarce federal resources" section of the 1990 Act when it notified the Senate and House Agricultural Committees in February 1992 that it does not plan to publish the report. This section requires the concurrence of both committees to not do studies and reports required by the act. To date, this concurrence has not been given.

Market Promotion Program highlighted how program funds can be wasted when more money is available than can be effectively used.⁶

CONFUSION OVER HVP EXPORTS' ECONOMIC BENEFITS

As I stated earlier, we believe there are good reasons for the government to be interested in promoting the export of HVPs. However, there is considerable confusion over the nature of the economic benefits of HVP exports. Although a 1989 ERS staff study, Exporting Processed Instead of Raw Agricultural Products, is frequently cited to support the proposition that the economic benefits of HVP export promotion exceed those of bulk exports, we think that its analysis does not support such a conclusion. The claimed benefits are based on key assumptions that render the study's conclusions unrealistic, and the study should not be used as the primary basis for government export assistance for HVPs.

The ERS study concluded that if its assumptions hold, a "prize" awaits a nation that successfully exports HVPs. For example, if, instead of exporting \$1 million of wheat, the United States turns that wheat into flour that is then exported, the domestic economy might gain \$9 million in business activity, employment for 109 workers, and increased tax revenues. However, the ERS study qualifies its conclusions by stating that the computed output and employment effects should be viewed as potentially available and represent the maximum effect of increased exports.

The requirements for achieving this maximum effect are stringent and unlikely to be realized. First, for its computations, ERS assumed that the United States would face a new and permanent increase in HVP export demand. However, as the study pointed out, there is no assurance that just because the United States wants to export more processed products other countries will buy them. Second, ERS assumes that all the inputs, including capital, infrastructure, and any labor needed to transform a bulk commodity into an HVP export, are currently unemployed. With this assumption, HVP exports can be increased without affecting input prices or taking inputs away from other sectors of the economy. The ERS study assumes that there is no opportunity cost to increasing HVP production and exports, i.e., no other production will have to be given up. Simply put, the alleged gains from an

⁶U.S. Department of Agriculture: Improved Management Could Increase the Effectiveness of Export Promotion Activities (GAO/T-GGD-92-30, Apr. 7, 1992); U.S. Department of Agriculture: Management Issues Remain Unresolved in the Market Promotion Program (GAO/T-GGD-92-25, Mar. 25, 1992); Agricultural Trade: Improvements Needed in Management of Targeted Export Assistance Program (GAO/NSIAD-90-225, June 27, 1990); and Agricultural Trade: Review of Targeted Export Assistance Program (GAO/NSIAD-88-183, May 24, 1988).

increase in HVP exports in place of bulk exports is derived entirely from the assumed productive efforts of unemployed workers and capital. With such an analytical approach, the most economically beneficial export will always be the one that uses the most unemployed resources.

CONCLUSION

In conclusion, we believe that promoting HVPs has merit. But, the amount of federal funds to be spent on HVP assistance and how they should be used should not be determined in isolation. What we think is most important is that a long-term agricultural trade strategy be developed and integrated into a comprehensive, governmentwide export promotion plan in order to assure that public resources are effectively used.

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Mr. Chairman and Members of the Subcommittee, this concludes my prepared statement. I will be happy to respond to any questions that you may have.

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